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ECONOMIC TRENDS

341

AND THEIR IMPLICATIONS FOR THE UNITED STATES

Prepared by Foreign Service Economic-Commercial Staff

CHIEF

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KEY ECONOMIC INDICATORS: CHILE, JUNE 1, 1967

Part II (Past Year)			Percent Change	
			1967 over 1966	1967 over 1965
Private money supply (millions of escudos)	average, Jan-Apr	1,557.5	+22.8	+24.2
Interest rate, current (annual %)	average, Jan-Jan	14	-	+4.0
External debt service ratio	estimated year-end	26.7	-12.0	+27.0
Gold and foreign exchange assets	Mar 31 of each year	+121.4	+58.8	-11.7
Balance of payments surplus (+) or deficit (-) (millions of \$)	estimated year-end	+21.8	-	-
Unemployment rate (%)	average, March	4.7	+21.0	-11.1
Indexes:				
Consumer price (1956 = 100)	average, April	211.1	+17.0	+22.3
Wholesale price (1956 = 100)	average, March	210.4	+19.2	+20.7
Industrial production (1960 = 100)	average, February	138.4	+2.8	+4.7
Basic wages (April 1953 = 100)	average, January	628.2	+37.7	+28.9
Imports and Exports:				
FOB (millions \$)	January-September	324.9	-	-
FOB (millions \$)	January-September	321.3	+20.0	-
Total imports, CIF (millions \$)	Annual data	783.2	n.a.	-
Imports from USA, CIF (millions \$)	Annual data	297.8	n.a.	-
Exchange Rates: Escudos per \$U.S.				
Bankers market (buying rate)	as of end of May	3.86	+23.4	+27.4
Bankers futures market (buying rate)	as of end of May	3.92	+22.5	+37.4
Brokers market (buying rate)	as of end of May	4.53	+15.2	+41.0

Source: Central Bank, CORFO, Ministry of Finance, Statistical Office, Customs, ENDESA.

SUMMARY

1. Growth in 1967 was substantially below level of 1966. Major weaknesses in construction and industries related to construction. Unemployment rate was up slightly in 1967, but recent data indicate improvement for 1968. A higher rate of growth is expected in 1968.

2. The long, six-month, legislative wrangle on 1968 wage increases for public and private sectors, now resolved, has undermined confidence in Frei Administration's price stabilization program. Annual increases in consumer and wholesale price indices to date are higher in 1968 than in 1967. Money supply expanded 28 percent in 1967 compared with 43 percent in 1968.

3. Price of copper remains at high levels and provides favorable outlook for Chile's balance of payments in 1968. Copper expansion program (one-half billion dollars) fully under way. The rate of growth of imports is expected to decline in 1968 from the 1966 and 1967 rates.

4. Business confidence is under the shadow of upcoming 1969 and 1970 elections. There was an upswing in new credits in 1967, from both U.S. and European lenders.

A. CURRENT ECONOMIC SITUATION AND TRENDS

1. Scant Growth in 1967. Although Chilean national accounts data for 1967 are not yet available, we expect that the final data will reveal a rate of growth in real (deflated) Gross Domestic Product between 2.5 and 3.5 percent. This compares unfavorably with the 5.3 percent annual growth rate attained in the 1964-1966 period (deflated and adjusted for improved terms of trade of Chile with the rest of the world). The basic productive sectors--agriculture, mining, and industry--account for 46 percent of Gross Domestic Product. Data for the 1964-1966 period indicate annual average rates of growth of 3.8 for agriculture, 5.3 percent for mining, 6.7 percent for industry, and 5.7 percent for these three sectors in aggregate. Best available data suggest 1967 growth in output of approximately 3.0 percent for agriculture, 2.0 percent for industry, and 3.0 percent for mining. Major important factors accounting for the 1967 slow-down were: (1) the using up of installed industrial capacity, (2) lack of prior expansion in copper mining, (3) decrease in construction activity, and (4) a somewhat more restrictive monetary policy than in 1965 and 1966.

2. Outlook for Economy in 1968 - Improvement. Favorable indications for improved performance in 1968 already exist for agriculture and mining. Substantially increased imports in 1966 and 1967 of machinery and equipment for expansion of industry suggest reduction in bottlenecks in the industrial sector in 1968. Construction starts (and government policy favoring housing construction) also suggest resumption in demand for the materials industries. A higher rate of industrial production in 1968 appears feasible. Therefore, on balance it is reasonable to expect an overall growth of Gross Domestic Product of 4.0 percent or more for 1968.

3. President Frei's State of the Union Message -- Guarded Optimism. President Frei presented his Fourth Annual Message to the National Congress on May 21. The President noted that a slowdown in economic growth had occurred in 1967 but that the three-year growth target of his Administration had been attained and that political differences should not be allowed to keep the program from getting back on track. He also noted that Chile's additions to external indebtedness in 1965-1967 were less than in 1962-1964, and that the dependence of the GOC's budget on external resources had been reduced.

Turning to agriculture, he noted that arable land under irrigation is being expanded as a consequence of numerous projects under construction and other projects being initiated. In reviewing the progress of agrarian reform, Frei noted that existing owners will be able to retain 50 basic irrigated hectares (approx. 200 acres) except in "very exceptional cases" where abandonment or notoriously poor exploitation is shown and that the GOC policy is not to expropriate "those farms, no matter how large, that exploit this land at a high technical level and under splendid social conditions."

4. Industrial Production - 1967 Slowdown. In 1967 industrial production increased by approximately 1.5 to 2.2 percent. Existing indices of industrial production are weighted in favor of slower growth in consumer goods and were appropriate to the 1950's. A composite index constructed by U.S. Embassy-AID indicates a rate of growth of 1.6 percent for 1967 as compared with 10.5 percent for 1966 and 8.6 percent for 1965. Industries supplying construction activity suffered the largest decrease in production in 1967. Production of consumer goods industries - food products, textiles, tobacco, footwear and clothing, furniture, publishing - advanced by 3.1 percent in 1967 as compared with 9.6 percent and 5.2 percent in 1965 and 1966. A major limitation on expansion of consumer goods was the lack of physical capacity. Substantial imports of machinery in 1967 should produce a turn around in these industries in 1968. Construction project initiation in 1967 exceeded the 1966 rate by 30 percent; the main impact on intermediate industry will probably be felt by the second half of 1968. On balance the advance of overall industrial production in 1968 will probably exceed the 4.0 percent mark. Production of intermediate industries--wood products, paper, leather, rubber, chemicals, coal and petroleum, non metallic minerals and primary metals--in aggregate underwent a decline of 1.2 percent in 1967, as compared with growth of 4.2 and 3.0 percent respectively in 1965 and 1966. Production of mechanical goods - fabricated metal products, machinery, electrical apparatus, and transportation equipment - advanced by only 3.5 percent in 1967 as compared with increases of 15.5 and 14.8 percent in 1965 and 1966. In 1967, intermediate and mechanical goods production appear to have been affected both by decreased construction activity and by bottlenecks in consumer goods industries.

5. Agriculture - Growth in Production Continues. Preliminary U.S.D.A. data for 1967 indicate a 2.8 percent increase in Chile's agricultural production. Relatively good weather conditions have also prevailed during the 1967-1968 harvest season. Wheat and sugar beet production in 1968 will undoubtedly exceed 1967 levels. Oilseed production is down from 1967 by 10- to 15 percent. Milk production in south central Chile appears to be increasing. Beef production is expected to be about the same as or less than in 1967. In regard to longer term trends, the hybrid corn-poultry revolution is now in full swing in Chile; in 1967 compared with 1966 corn production rose 47 percent and poultry meat production rose 41 percent. Sugar beet production also scored a high gain -- 31 percent in 1967. Production in 1967 of barley, oats, dry beans, lentils, onions, and rapeseed declined as compared with 1966 production. Chile has been a substantial net (and gross) importer of beef (live and on-the-hoof), wheat, sugar, and powdered milk. While 1967 and 1968 crop results are encouraging, they lessen this dependence on imports only slightly.

6. Agrarian Reform Progress Report. Since the beginning of 1967 the Agrarian Reform Corporation (CORA) has made steady progress in its

program to redistribute agricultural land to the campesinos that work it. During this period CORA expropriated 286,000 hectares, of which 61,000 were irrigated, and settled 4,307 families in 159 new asentamientos. This brings the total during the Frei administration up to 1,236,000 hectares expropriated (157,000 irrigated) and 8,427 families settled on 248 asentamientos.

7. Strikes and Labor Unrest - Employment. With the exception of construction industry and regional food, employment through the first half of 1968 has been relatively high. The unemployment rate in Santiago was 5.1 percent in 1967 compared with 5.4 percent in 1966. Recent data (March 1968) indicate a decline of the rate to 5.6 percent. According to Ministry of Labor data, in 1967, total man days lost to strikes were 1,284,000 as compared to 1,261,000 man days in 1966. Thus far in 1968, public sector employees constitute the main source of strike activity. Thus far, postal workers (42 days out), teachers (56 days out), state airline, petroleum, and maritime employees have been on strike. Telephone, electrical, textile workers also struck for varying periods. Steel workers are presently on strike. Strikes of public employees were motivated in most instances to obtain special wage increases while wage readjustment legislation wound its way through an extremely slow legislative process. With readjustment and an accelerated pace of inflation, it is expected that organized labor will bargain to exceed the 21.9 percent CPI increase plus productivity increases. Business management resistance, stiffened by tight credit conditions and weakening demand, explain, in part, present labor unrest.

8. Prices - Some Acceleration. By December 1967, the Santiago Consumer Price Index (CPI) was 21.9 percent above the December 1966 level. Wage readjustments for public sector employees in 1968 have been linked, as in the past three years, to the December-to-December increase in the CPI of the preceding year. Through May 1968, the CPI has advanced 15.5 percent, as compared with 12.1 percent for the same period in 1967.

9. External Sector - Renewed Strength of Copper. Copper exports in recent years have constituted 70 percent of Chile's commodity export earnings. The averaged price per pound for Chilean copper in world markets increased from 37.5 cents in 1965 to 47.6 cents in 1966 to 48.5 cents in 1967. The copper windfall bolstered Chile's international reserve position by \$122 million in 1966, as well as permitting a \$156 million increase in imports in 1966. In 1967 the higher import level combined with a sharp reduction in capital inflows resulted in a reduction in Chile's international reserves in spite of the high copper price. Chile's deficit (compensatory) on balance of payments for 1967 was \$25.5 million. However, the reduction in commercial arrears of a term of more than 120 days and in the importer's waiting period for

foreign exchange to sixty days (in some cases 50 days), accounted for a \$40 million use of foreign exchange. Through the first five months of 1968 the (London) futures price for copper has averaged approximately 58 cents per pound. Therefore, in spite of the decline in the copper price to the 45-50 cent range, the average price for copper this year, and, in turn, Chile's export earnings from copper, can be expected at a level close to that obtained in 1967.

10. Copper Expansion Program Underway. Production of copper in 1967 totalled 661 thousand metric tons, a 3.8 percent increase over 1966. Total new investment authorized under Chilean decrees for copper mining in the present expansion program is \$467 million, which will be made over a four to five year period. Approximately \$76 million was invested in 1967 (of a total \$93 million to the end of 1967). Approximately \$40 million of the 1967 investment was for imported goods and services and \$35 million for expenditures in Chile - mainly mine construction activity. Production of copper by 1970 is expected to be 25 percent above 1968 production and by 1972 the increase over 1968 will be approximately 50 percent.

11. Increase in New Credits. Preliminary data for 1967 indicate that Chile received \$508 million in new credit and loan agreements, as compared with \$336 million in 1966 (both data exclude suppliers' credits not identified by source). The Export-Import Bank signed loan agreements totaling \$250 million in 1967, the bulk of which will be drawn upon to finance Chile's one-half billion dollar copper expansion program. New loans authorized by international lending organizations--the IBRD, IDB, and IMF--declined from \$160 million in 1966 to \$40 million in 1967. New credit agreements negotiated with European public and quasi-public lenders increased from \$34 million in 1966 to \$80 million in 1967. New AID loan authorizations amounted to \$68 million in 1967 as compared with \$92 million in 1966. Data prepared by CORFO on the expected state of Chile's external debt service as of December 31, 1966 indicated an impending burden of debt service for 1967 amounting to \$242 million and \$260 million for 1968. Data prepared by CORFO as of December 31, 1967 indicate an impending burden for 1968 of \$285 million for 1968 and \$188 million for 1969. Even though these data will be altered by new credit agreements in 1968, they suggest that a sizeable decline can be expected in foreign exchange requirement for service of outstanding debt for 1969.

12. Chilean Conference on Production and Trade. The Chilean Private Sector climaxed six months of organizational effort with a national Convention of Production and Trade in Santiago April 1-4, 1968. The Convention was attended, at one time or another, by some 9,000 delegates who came from all over Chile to voice their concern over the general economic situation in Chile. A few delegates also came

from abroad. While there were some attacks on Government policy at the meetings, the Convention's apolitical nature was set when President Frei addressed the opening session with an appeal for support by the Private Sector.

After the opening day ceremonies, the Convention broke up into 19 working groups, committees or subcommittees who prepared resolutions or recommendations such as the following: preparation of a national industrial plan, a slow-down in the agrarian reform program, a reduction in charges and controls on private trade, an increase in public works and other construction, creation of a National Private Transport Agency, a relaxation of credit restrictions on banks, a plan for installment sales of stocks, a recommendation to raise the tourist office to the rank of subsecretariat, a plan for expanded worker training programs, greater business participation in LAPTA and ANDINA regional integration processes, a conciliation service to help settle strikes and a general declaration of the proper role of the business enterprise and Government in the economic processes.

Reportedly the Convention's recommendations were sent to the Government and were also published for general dissemination. The Convention received ample press coverage. Since the close of the meetings, however, there has been only a minimum of follow-up activity.

B. IMPLICATIONS FOR THE UNITED STATES

1. Prospect for Recovery in 1968. The economy this year shows signs of recovery from the slow-down of 1967. It should be noted that 1965 and 1966 were good years in which sizeable increases in incomes of the lower income groups increased demand for consumer goods. Relatively high levels of imports of capital goods in 1967 suggest easing in limitation of industrial capacity which impeded achievement of a higher growth rate in 1967.

2. Future of Price Stability-Uncertain. Even mild acceleration of inflation in late 1967 and early 1968 augurs ill for the future of Chile's stabilization program. It is too early to judge the full impact of the recent wage readjustment legislation on Chile's fiscal and monetary programs. The fact that this legislation includes measures to increase government revenues suggests that the government still intends to hold inflation to manageable rates.

3. Influence of 1969 and 1970 Elections. The March 1969 Congressional election and 1970 Presidential election already influence political activity, and this may lead to strong campaign statements. The basic tenets of the Government--for social change, stabilization within manageable levels, an important role for private enterprise, agrarian reform but also higher agricultural prices, expansion of educational opportunity, copper expansion--have not altered.

4. Increasing Foreign Trade Competition. The flow of foreign credits into Chile is continuing. The availability of credits from European sources is exerting strong competitive pressure on U.S. exporters for the Chilean market. The U.S. share of Chile's imports for all of 1967 is still not known.

5. Balance of Payments and Imports. The prolonged eight month strike in the U.S. copper industry sustained copper prices at high levels in late 1967 and early 1968. As a result, Chile did not suffer a major deficit on balance of payments in 1967. On the other hand, Chile's commodity imports increased substantially in the last two years, rising from \$626 million in 1965 to \$783 million in 1966, and to \$830 million in 1967. It is unlikely that the 1968 import bill will be any less than in 1967. Even so, at this time, no major deficit or surplus in the balance of payments is in sight for 1968.